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TAGS: ECON EINV EFIN ETRD BEXP KTDB PGOV SF
SUBJECT: SOUTH AFRICA ECONOMIC NEWSLETTER
NOVEMBER 26, 2004 ISSUE

¶1. Summary. Each week, AMEmbassy Pretoria publishes an economic newsletter based on South African press reports. Comments and analysis do not necessarily reflect the opinion of the U.S. Government. Topics of this week's newsletter are:
- October Consumer Prices Slightly Higher than Market Expectations;
- Producer Prices Show Mild Gain;
- BER Expects SA Growth to Exceed 4 Percent in 2005;
- Limpopo Study Aims to Increase Food Production;
- Leading Economic Indicator up 9.3 Percent;
- Erwin Clarifies Listing of New State IPOs;
- Interest Rate Reduction More Likely in Early 2005;
- Signs of Strong Domestic Investment; and
- Over Half of South Africans are Living in Poverty.
End Summary.

OCTOBER CONSUMER PRICES SLIGHTLY HIGHER THAN MARKET EXPECTATIONS
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¶2. In October, targeted inflation (CPIX, consumer prices excluding mortgage costs) increased by 4.2 percent (y/y), slightly higher than the 4.1 percent growth Reuter's market consensus forecast. October's overall consumer prices increased by 2.4 percent (y/y) compared to September's growth of 1.3 percent. Higher food, fuel and power and transport prices were why October's CPIX inflation was higher than September's 3.7 percent. Rising meat, fruit and vegetable prices pushed up food costs in October and food prices are expected to rise as a result of adverse weather conditions (drought has lasted over two years) and rising global food prices. Source: Standard Bank, CPI Alert, November 24; Business Day, November 25.

PRODUCER PRICES SHOW MILD GAIN

¶3. October producer prices increased 1.9 percent (y/y), slightly higher than market expectations of 1.8 percent and an increase of 0.5 percentage points over September's producer price inflation. Domestic producer prices increased 2.7 percent while imported producer prices showed a 0.3 percent decline. In October, the sharp increase in oil prices contributed 0.6 percent to the month/month increase in producer price inflation, with oil price contribution strong in plastics, chemicals and petroleum products. Increases in oil prices in the domestic economy should be lower in November as the rand remains strong and the global oil prices have retreated from recent highs. Source: Investec, PPI Update; Standard Bank, PPI Alert, November 25; Business Day, November 26.

BER EXPECTS SA GROWTH TO EXCEED 4 PERCENT IN 2005
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¶4. The University of Stellenbosch's Bureau for Economic Research (BER) expects South African economic growth to exceed four percent in 2005, helped by strong consumer and investment demand. Although growth should be higher than this year's expected 2.9 percent, exports should show slow growth next year because of the rand's strength. BER expects that growth in consumer spending would slow next year to around 3.7 percent down from 4.1 percent in 2004, while investment was set to increase by 9 percent next year compared to 8.4 percent this year. BER forecasts the rand to weaken to around R7.50-R8 against the dollar in 2005, given South Africa's widening current account deficit. Economist Mike Schussler forecasts that growth will rise above 4 percent over the next two years, with record growth in economic activity likely to continue until 2010, when South Africa hosts the Soccer World Cup. Source: Business Day and I-Net Bridge, November 19.

LIMPOPO STUDY AIMS TO INCREASE FOOD PRODUCTION
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¶5. Half of Africa's population will face water stress or scarcity by 2025. For the next five years, researchers will study the way farmers along the Limpopo basin through Zambia, Botswana, Zimbabwe, Mozambique and SA collect and manage water. The $5 million World Bank-funded research project will examine how the river basin could be a more reliable producer of food for the 14 million people surrounding the river. According to Adriaan Louw of the South African Agricultural Research Council, which is coordinating the research project, about 10 percent of the population was expected to abandon their homes and migrate south in the next five years. The poverty of people living in the Limpopo basin makes them susceptible to failures in the water supply. In dry years, some stretches of the river only see water flowing for 40 days and pollution and competition for usable water can prevent efficient use. The Limpopo is one of nine river basins the researchers will study. As well as gathering information about the problems, they will introduce different farming methods to ensure better management of soil and water. Small farmers, who rely on seasonal rains making them vulnerable to the frequent floods and droughts, do much of the farming in the Limpopo basin. Source: Business Day, November 19.

LEADING ECONOMIC INDICATOR UP 9.3 PERCENT

¶6. South Africa's September 2004 leading economic indicator rose by 9.3 percent (y/y), according to the South African Reserve Bank (SARB), compared to August's y/y change of 10.7 percent. In September, four leading indicator components showed slower growth and three showed higher. Interest rate spreads between the money market and capital market instruments, commodity prices, and the leading indicator of major developed countries contributed to slower September growth while job advertisements, average manufacturing hours worked, equity prices and real M1 money supply growth showed higher growth. The coincident indicator is up 20.2 percent y/y in August compared to 18.7 percent y/y in July. This increase reflects the strong growth in domestic activity and is at its highest y/y growth since 1995. In March 2004, the SARB revised its leading and coincident business cycle indicators. The SARB first published business cycle indicators in 1983. These indicators were revised in 1994 and have now been revised again. The leading indicator has been reduced to 13 components from 21, while the coincident indicator has been cut to 5 from 7. The new indicators are less volatile than the old indicator, while the lead for the leading indicators has been extended to 15 months from the previous 11.5 months at the peak and five months at the trough. Source: I-Net Bridge November
¶22.

ERWIN CLARIFIES LISTING OF NEW STATE IPOS

¶7. Public Enterprises Minister Alec Erwin launched this week the IPO Reference Manual, a guide for upcoming share sales of state assets. The Public Enterprises Department said it viewed IPOs as one option available in the restructuring of state-owned enterprises. Erwin said parastatals would need to meet conditions for listing. "An IPO would be considered when the corporate structure and balance sheet of the state-owned enterprise is strong, and where we see the opportunity of lowering the cost of capital through an IPO; however, no IPOs are envisaged this financial year," he said. He expects concessions, joint ventures and public-private partnership arrangements to continue in the next year. Although government would retain strategic control of power utility Eskom, national carrier South African Airways and Transnet, parts of these parastatals could be partially listed as their balance sheets and corporate structures become stronger. Airports Company SA (ACSA), which owns and operates 10 of South Africa's major airports, will be sold next year. ACSA was the first parastatal to be partially privatized when Italian operator Aeroporti di Roma paid R918 million for its 20 percent share in 1998. The transport department has scheduled a shareholders' meeting for December to discuss the sale of shares in the company and details should be announced by the end of the year. Aeroporti di Roma is expected to exercise its option to buy another 10 percent in the company. Government owns 76 percent of ACSA, while five empowerment consortia collectively own 4 percent. Source: Business Report, Business Day and I-Net Bridge, November 23.

INTEREST RATE REDUCTION MORE LIKELY IN EARLY 2005
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¶8. The next South African Reserve Bank's Monetary Policy Committee (MPC) meeting, scheduled for December 8 and 9, promises to surprise either financial markets or economists, reflecting divided views. The MPC could cut the repurchase rate by 50 basis points, as reflected by

forward rates, which are now pricing in close to a 100 percent probability of a 50 basis point rate cut. Alternatively, the bank may leave rates unchanged. The Reuters consensus forecast indicates that most economists believe this will be the outcome. The major factor in support of a rate cut is the low inflation rate, which has been supported by the strong rand. CPIX, the bank's official inflation measure, reached a low of 3.7 percent in October, and although it is expected to increase from this level, there is consensus that it will remain within the target range of 3 percent to 6 percent in the next two years. The currency broke the key R6 to the dollar level this month, supported by improving South African macroeconomic variables and dollar weakness. Reuters forecasts indicate that most economists believe the rand will weaken steadily in the near to medium term. If currency strength persists, there is a risk the bank might undershoot the inflation target. However, the bank has explicitly said it would not intervene, so it seems a rate cut may be the only option available to weaken the currency. Factors not supportive of another rate cut include continuing strong consumer demand and high oil prices. Over the past few months there has been a retail and vehicle sales point to robust consumer demand. Private sector credit extension is at high levels, meaning consumers are borrowing in order to spend, and this tends to be inflationary. Since consumer demand is normally quite high during December, it implies that an interest rate cut at this meeting would add fuel to consumer spending and credit demand. For these reasons, analysts believe that the MPC will wait until early 2005 to change interest rates, even with a strong currency. Source: Business Day, November 23.

SIGNS OF STRONG DOMESTIC INVESTMENT

¶9. Domestic fixed investment shows signs of increasing at record levels over the next several years. The announced private sector investment plans include: R 5 billion ($830 million using 6 rands per dollar) over the next five years by SAB (part of SABMiller), SASOL (an oil company) with capital spending at R 15 billion ($2.5 billion), PPC (a cement company) spending R1 billion ($170 million); and investment by vehicle manufacturers reaching a five-year high of R3.5 billion ($580 million) in 2004. Public enterprise investment spending should also increase briskly. Eskom (the electricity parastatal) and Transnet (transportation public enterprise) are expected to spend R165 billion ($27.5 billion) improving South Africa's infrastructure. Source: Business Day, November 23.

OVER HALF OF SOUTH AFRICANS ARE LIVING IN POVERTY
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¶10. Fifty-seven percent of South Africans are living below the poverty line, according to a recent study by the Human Sciences Research Council (HSRC). Based on data gathered in the 2001 census, the report said the provinces with the highest proportion of poor people were Limpopo (77 percent) and Eastern Cape (72 percent). Western Cape and Gauteng had the fewest proportion of poor with 32 percent and 42 percent, respectively.

The poverty gap, which is the amount it would take to bring the income of the poor up to the poverty line, increased from R56 billion in 1996 to R81 billion currently. KwaZulu-Natal, at R18 billion, has the largest poverty gap, followed by Eastern Cape and Gauteng. Gauteng's poverty gap grew faster than other provinces because the area's population has grown faster than its economy. The poorest municipality was Ntabankulu in the Eastern Cape where 85 percent of people lived below the poverty line. Municipalities with the lowest poverty rates included Stellenbosch (23 percent) and Saldanha Bay (25 percent) in Western Cape. Of the large cities, Cape Town had the fewest poor people at 30 percent, followed by Pretoria (35 percent) and Johannesburg (38 percent). Source: Sunday Times, November 21; Allafrica.com, November 23.

¶11. Comment. The HSRC study's poverty line is based on the Bureau of Market Research's minimum living level in
¶2001. The poverty line varies according to household size; the larger the household, the larger the income required to keep it out of poverty. The poverty income by household size in 2001 used in this study was:

Household Size, Rands per Month (6 rands per $)

1	587 ($98)
2	773 ($129)
3	1028 ($170)
4	1290 ($215)
5	1541 ($257)
6	1806 ($300)
7	2054 ($340)
8+	2503 ($417)

End comment.